

# Physical Inventory Guidelines

## Purpose

This document provides guidelines for conducting annual physical inventories, and is applicable to all units that hold inventory for resale to external or internal customers. Annual physical inventories not only help ensure the accuracy of inventory balances reported in the University's financial records but also help you manage the activity in your area.

While these guidelines address annual physical inventories, similar concepts apply to cycle counting, but the specific steps are different. Cycle counting is a process that uses regularly scheduled counts but does not count the entire inventory in a single event. Please contact the Controller's Office Business Operations Department at 3-0781 for guidance.

The document consists of the following sections and supplemental information in the appendices.

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## Responsibilities

The Finance or Business Manager of the unit is responsible for ensuring the annual physical inventory is properly performed, inventory records reflect actual quantities on hand, inventory valuation methods are appropriate, and adjustments are entered in the University's accounting system on a timely basis.

In addition, the Finance or Business Manager is responsible for ensuring that segregation of duties is maintained throughout the inventory process to promote the safeguarding of the assets, protection of employees, and objective reporting of inventory. Specifically, no one person should be able to authorize a transaction (e.g., a purchase or sale), record the transaction, have custody of the inventory, and perform the related reconciliation.

## Planning for a Physical Inventory

Time spent planning and preparing for the physical inventory will streamline the count process and reduce errors and rework.

- A. **Clearly define roles and responsibilities.** In general, the inventory counting process and the reconciliation should be *supervised or performed* by an independent person. This independent person should NOT be the person who checks in or receives inventory, maintains the inventory records for the items, or is responsible for the daily security and accountability of the inventory.

An example of participants' possible responsibilities follows:

1. **Manager:** plans and supervises inventory, makes test counts, approves adjustment journal.
2. **Staff Member #1:** tabulates physical count and identifies possible errors.
3. **Staff Member #2:** reconciles physical count to Oracle Financials; creates adjustment journal.
4. **Count teams:** count the stock on hand.

The number of people involved will depend upon the size and complexity of the organization and the items being counted.

- B. **Establish a master schedule** that sets the beginning and completion dates for both the counting process and the inventory reconciliation.
1. Physical inventories are typically done in the summer to allow sufficient time to reconcile and adjust balances before the August fiscal year-end close.
  2. For ease of reconciliation, consider scheduling the completion of the physical inventory count to coincide with the last working day of a period.
  3. Suspend all transaction activities such as receiving and sales during the count process to make the process more efficient.
- C. **Notify affected parties** providing adequate lead time to plan appropriately. For example,
1. Notify suppliers if deliveries will not be accepted during this time.
  2. Advise customers in advance of the shut-down period.
  3. Inform employees to allow them sufficient time to plan for the activity.
- D. **Purchase necessary supplies** before the count. Supplies might include:
1. Sequentially-numbered inventory tags (see sample in Appendix A) to be used to identify items that have been counted and how many times they have been counted. Consider preprinted tags, if available from your inventory tracking system, containing all of the information except the actual counts and team numbers, to reduce the effort on the day(s) of the count.
  2. Other supplies like name tags, pens, markers, clipboards, calculators, tape, scales, step stools.
  3. If needed, special materials for handling product, such as plastic gloves or masks.
- E. **Prepare the storage area** for the inventory count. (If the warehouse is clean and organized throughout the year, additional efforts before the count should be minimal.)
1. Clean all areas for ease of counting.
    - a. Make sure like items are grouped together.
    - b. Arrange items so they can be easily counted (i.e., in "batches").
    - c. Ensure there are no hazards in the warehouse that could be dangerous during the inventory count, such as boxes to trip over, wet floors, items that could fall, etc.

2. Organize the stock.
  - a. Clearly mark package quantities if necessary.
  - b. Count and seal partial packages with the count and date clearly marked. Cross out any conflicting information, like previous counts, different part numbers, etc., and ensure that the package has the correct part number clearly marked.
  - c. Clearly mark items that will not be counted with "DO NOT INVENTORY". Identify damaged goods and move them to a designated separate location.
  - d. Label each area to be counted. For example, label shelving units alpha-numerically (BA1, CD2) and each individual shelf numerically (top shelf = BA1-1, second shelf = BA1-2, etc.). In this way, you can create a complete list of all areas to be inventoried and "check off" each area as it is completed. Count each marked location separately.
  - e. Make sure all items are identified with a part number, bar code, or other identification.
  - f. Update storage area floor plans to reflect current stock locations and identify count areas.
  
- F. **Organize counting teams**. Physical inventories should be performed by personnel who have no direct responsibility for assets subject to the inventory count. If the use of such personnel is not feasible for any part of an inventory, then those portions should be tested and verified by an independent person.
  1. If supplemental resources are required, consider using staff from other areas or hiring Stanford students and temporary employees to supplement the unit staff.
  2. Define count teams with at least two members per team.
  
- G. **Develop written physical inventory instructions** for individuals participating in the count. Appendix B contains a sample of such instructions.

- H. **Establish clear cutoff guidelines**, identifying which items to include or exclude from the inventory count.
1. If possible, complete all handling and recording of inventory products before the physical inventory count begins. This includes receipts, returns, consolidation between stocking locations, etc.
  2. No movement of any inventory should be permitted during the physical count. Any items that are delivered during the count should be physically separated and labeled "POST INVENTORY: DO NOT COUNT".

If movement is required, backup documentation should be maintained and the quantity reflected in the count or subsequent discrepancy reconciliation. A good practice is to attach a count tag to copies of the documentation.

## Conducting the Physical Count

- A. **Review counting instructions** with the counting teams before they begin. Provide examples of how to find codes, units of measure, quantities, etc. Demonstrate an actual count. Explain the complete process, including reason for the count, storage area and stock layout, numbering and distribution of inventory tags, collection, and summarization of the count sheets.
- B. **Control of the inventory tags** or count sheets helps ensure completeness and accuracy of the count.
1. If inventory tags are used, confirm that each stack issued to count teams is complete and in numerical sequence. A log should be kept of the tags issued to each team to ensure all are returned and accounted for, otherwise a tag with a "real" count may be misplaced and you may not be aware of it.
  2. Complete inventory tags in pen to prevent erasures. Correct errors by lining out the error, writing the correct entry, and initialing the change. If an entire tag must be redone, the tag should be marked "ERROR – DO NOT COUNT" and a new tag created for the item. No inventory tags should be discarded.
  3. Collect the completed inventory tags from each team at the end of the second counts, confirming against the log that the same tags issued have been returned and that no tags are missing.

- C. **Count items twice** to provide as accurate a count as possible. Each count team should be assigned to a specific area for their first count, then perform a second count in another area to confirm that area's first count. Discrepancies should immediately be brought to the manager's attention. Third and fourth counts may be necessary to obtain an accurate count.

## Reconciling the Physical Inventory

Reconciliation is defined as the process of identifying, explaining, and correcting the differences between the physical count and the asset balance in the General Ledger (GL). It is easiest to reconcile after month-end close to ensure up-to-date information in Oracle Financials and ReportMart3. Appendix C contains a sample of an inventory reconciliation.

- A. **Determine the amount per physical count.**
1. Enter the physical count into an inventory control system (database), if there is one, or into a spreadsheet listing all items in the inventory.
  2. Significant discrepancies between the records and the count should be investigated and explained.
  3. Calculate the total inventory cost by multiplying units per count by unit cost.
  4. Adjust the value per the count by costs not included in the unit cost, where appropriate. For instance, if unit cost excludes sales tax or shipping charges, add those values to the inventory on hand since they are included in the GL balance.
- B. **Determine the amount per the General Ledger.**
1. Begin with the month-end inventory balance in the GL (object code 11405) per ReportMart3 Posted Journals Report (FIN\_GL\_161\_Post\_Jrnl\_By\_Obj\_Code). Use the month-end report and limit the result by object code to shorten the report. A sample report is included in Appendix D.

- 2. Increase the GL balance in the reconciliation worksheet by accounting for items received before, and included in, the physical inventory count but for which the purchase has not been posted. Two conditions must be considered:
  - a. The invoice has been received by Accounts Payable but payment has not been made and therefore will not be recorded until the next period. The Invoice Detail Report (FIN\_EXP\_138\_Invoice\_Detail\_Recon) will help identify these transactions. A sample report is provided in Appendix E.
  - b. The invoice has not been received by Accounts Payable or the invoice is "on hold". The Purchase Order Detail Report (FIN\_PO\_206\_AP\_Purch\_Order\_Detail) should be used to help identify these transactions. A sample is provided in Appendix F. This report may also be used during the year to monitor purchases and ensure prompt payment to suppliers.

C. **Determine the adjustment amount.** The difference between the amount per physical count and the amount per GL is the adjustment required to reflect the true amount in the GL. An adjustment journal must be created in Oracle Financials iJournals and routed for approval. A sample adjustment journal is included in Appendix F.

D. **Consider obsolescence.** Compare the quantity on hand to the quantity used or sold during the year:

	PHYSICAL COUNT, PREVIOUS YEAR
+	PURCHASES, CURRENT YEAR
-	PHYSICAL COUNT, CURRENT YEAR
=	QUANTITY USED, CURRENT YEAR

If the amount on hand greatly exceeds what was used during the year, you may have an obsolescence issue. Determine if excess quantities or obsolete goods exist and prepare an adjustment to write them off, similar to the inventory adjustment described above.

**Appendix**

**A: Sample Inventory Tag**

Available via Campus Wide Agreements, part number AVE153%.

|-----Count #2-----|-----Count #1-----|

TAG NO. <b>1796</b>		ARTICLE OR KIND OF MATERIAL			TAG NO.	
		A B			<b>1796</b>	
G I H		J COUNTED BY			UNIT * D	
AMOUNT H		AMOUNT G	SIZE E	COUNTED BY F	AMOUNT C	
LOCATION BLDG. SEC. FLOOR		PRICED-BY	CHECKED BY J	UNIT PRICE		
REMARKS					TOTAL VALUE	
DATE					DATE	
* Unit means Singles, Pairs, Pcs., Lbs., Fl., Yds., Gals., Reams, Etc. If notations are made on back mark X here _____ Enter only one item on tag. All tags must be accounted for.						

**Count #1:**

- A. Description of Item (Product Name)
- B. Stock # or Barcode # or Manufacturer Catalog #
- C. Quantity Counted
- D. Unit of Measure (box, each, pkg.)
- E. Location (listed on shelf, e.g., AB1, AB2)
- F. Team Number

**Count #2:**

- G. Description of Item
- H. Quantity Counted
- I. Unit of Measure
- J. Team Number (on both sections of the tag)



## B: Sample Instructions for a Physical Inventory

There will be two counts. Instructions for each count are different and are provided below:

**First Count.** We will have teams of two; each team will receive a stack of inventory tags:

- A. One person will count the item.
- B. The second person will record the count and item information on the inventory tag.
- C. The tag will be taped to the shelf where the item is located.
- D. Switch roles occasionally to stay sharp.

You are responsible and accountable for all tags assigned to you during the first count. Please use them in order and return any unused tags to the issuing staff member.

**The following will need to be indicated on the bottom half of the inventory tags. Refer to the Sample Inventory Tag for correct placement of each entry.**

- A. **Description of Item** (Product Name)
- B. **Stock # or Barcode or Manufacturer Catalog #** (Tag requires only ONE of these. We prefer that you list them in the order above. If you cannot find the stock #, look for the barcode; if there is no barcode, look for a catalog #. Do not list all four numbers.)
- C. **Quantity Counted**
- D. **Unit of Measure** (box, each, pkg.)
- E. **Location** (listed on shelf, e.g., AB1, AB2)
- F. **Team Number**

**If your team is unsure of any of the needed information for the tags, please see a supervising staff member.**

Once your team has completed the first count for the shelves or area which you have been assigned please see a supervisor for assignment to a second count area.

**Second Count.** After all first counts of inventory have been completed, your team will be assigned to a different location to verify its first count. Teams will count items and compare it to the first count made. Once it has been verified, the team will complete the top portion of the tag with the following:

- G. Description of item**
- H. Quantity Counted**
- I. Unit of Measure**
- J. Team Number** (on both sections of the tag)

Your team will tear off the bottom portion of the tag and submit them in numerical order to the supervisor for data entry after you complete your second count. If your team finds ANY discrepancies during your second count please notify a supervisor immediately.

**C: Sample Inventory Reconciliation**Inventory Per Physical Count

Inventory On Hand, 30-JUN-20XX	\$ 664,453.16 <sup>a</sup>
Sales Tax @ 8.25%	<u>54,817.39</u> <sup>b</sup>
<b>TOTAL INVENTORY ON HAND, 30-JUN-20XX</b>	<b>\$ <u>719,270.55</u></b>

Inventory Per Oracle Financials General Ledger

General Ledger Inventory per Report 161 Posted Journals	\$ 528,004.00 <sup>c</sup>
Items received by 30-JUN-20XX but not on GL until after 30-JUN-20XX:	
A. Invoices unprocessed at month-end	\$ 92,784.65 <sup>d</sup>
B. Receipts not invoiced	<u>108,139.62</u> <sup>e</sup>
<b>TOTAL ADDITIONS</b>	<b>\$ 200,924.27</b>
<b>TOTAL ADJUSTED INVENTORY PER ORACLE FINANCIALS, 30-JUN-20XX</b>	<b>\$ <u>728,928.27</u></b>
 <u>Difference Between Count and General Ledger</u>	 <b>\$ <u>(9,657.72)</u></b>

<sup>a</sup> e.g., "Physical count of inventory, extended at unit cost"

<sup>b</sup> e.g., "Sales tax not included as part of unit cost"

<sup>c</sup> e.g., "Year-to-date total of entries for object code 11405 posted to award  
AAAAA"

<sup>d</sup> e.g., "Per Report 138 Invoice Detail, total of all invoices received by Accounts  
Payable but paid in a GL Period after JUN-20XX"

<sup>e</sup> e.g., "Per Report 206 Purchase Order Detail, total of all purchase orders  
received with no invoice or invoice on hold as of 30-JUN-20XX"

D: Sample Report 161 Posted Journals

Project	Award	Object	Journal	Li #	Jrnl Line Desc	Date	Jrnl Debit Amt	Jrnl Credit Amt	Beginning/Ending Balance						
<p>Run Date: 28-JUL-20XX 10:30 AM                      Last Close: JUN-20XX</p> <p style="text-align: center;"><b>STANFORD UNIVERSITY</b>                      Posted Journals By Object Code                      Excluding Orgs                      For the Period Ending June 30, 20XX</p> <p style="text-align: right;">Page: 1 of 2                      User: GWD                      Database: DW2_PRD;</p> <p>Report Prompts:</p> <table border="1"> <tr> <td>001: Project Number %</td> <td>003: Set of Books SU</td> <td>100: Award Org or Parent Org %</td> </tr> <tr> <td>002: Award Number AAAAA</td> <td>004: Object Code 11405</td> <td>200: Period JUN-20XX</td> </tr> </table>										001: Project Number %	003: Set of Books SU	100: Award Org or Parent Org %	002: Award Number AAAAA	004: Object Code 11405	200: Period JUN-20XX
001: Project Number %	003: Set of Books SU	100: Award Org or Parent Org %													
002: Award Number AAAAA	004: Object Code 11405	200: Period JUN-20XX													
<b>11405 - INVENTORY</b>															
1111111 - AAAAA - 11405									569,590.73						
			jj0123456 i	1	Sales Tax	06/30XX	0.00	3,363.94							
			jj0789012 i	2	SubTotal	06/30XX	0.00	41,103.02							
			jj0345678 i	1	Sales Tax	06/28XX	0.00	930.30							
			jj0901234 i	2	SubTotal	06/28XX	0.00	11,320.08							
			jj0567890 i	1	Sales Tax	06/30XX	0.00	22,366.12							
			jj0234567 i	2	SubTotal	06/30XX	0.00	272,167.31							
			Payments US	2	Journal Import Created	06/20XX	0.00	7.59							
			Payments US	3	Journal Import Created	06/01XX	0.00	4.60							
			Payments US	3	Journal Import Created	06/29XX	0.77	0.00							
			Payments US	4	Journal Import Created	06/12XX	0.00	13.76							
			Payments US	4	Journal Import Created	06/26XX	0.00	5.48							
			Payments US	4	Journal Import Created	06/27XX	0.00	2.39							
			Payments US	5	Journal Import Created	06/28XX	0.00	0.80							
			Purchase In	1	Journal Import Created	06/17XX	10,343.42	0.00							
			Purchase In	2	Journal Import Created	06/01XX	3,974.94	0.00							
			Purchase In	2	Journal Import Created	06/10XX	11,733.05	0.00							
			Purchase In	2	Journal Import Created	06/11XX	275.37	0.00							
			Purchase In	2	Journal Import Created	06/19XX	4,908.21	0.00							
			Purchase In	2	Journal Import Created	06/23XX	705.14	0.00							
			Purchase In	2	Journal Import Created	06/26XX	18,999.31	0.00							
DATA NOT SHOWN															
			Purchase In	20	Journal Import Created	06/05XX	0.00	0.01							
			Purchase In	21	Journal Import Created	06/08XX	0.00	0.02							
			Purchase In	22	Journal Import Created	06/09XX	0.00	0.02							
<b>Total For: 1111111 - AAAAA - 11405</b>							<b>151,375.91</b>	<b>109,789.18</b>	<b>528,004.00</b>						

Document Name: FIN\_GL\_161\_Post\_Jrnl\_By\_Obj\_Code.rep - Report tab name: Journals w/o Orgs

### E: Sample Report 138 Invoice Detail

Invoice: 60264603  
 Supplier Name: %  
 Supplier Number: %  
 Supplier Sites: %  
 Project #: %  
 Project-Task: %  
 Award: %  
 Expenditure: %  
 GL Period: %  
 Invoice Creation Dates from: % to %  
 Supplier Invoice Dates From % to %

**STANFORD UNIVERSITY**

**INVOICE DETAIL RECONCILIATION REPORT - FULL DISPLAY**

Page: 1 of 1  
 Run Date: 03-JUL-20XX  
 User: GWD  
 Database: Production

  

**Invoice Header and Supplier Information**

Invoice Number	Invoice Date	Invoice Amount	Supplier Name	Supplier#	Supplier Site	Attachment Y/N	Invoice Terms
60264603	08-Jun-20XX	2,460.62	SUPPLIER	Supplier #	CWA_PAY		N30

  

**Invoice Distribution Information**

Line #	Line Item	Line Amount	Expenditure Date	GL Date	Invoice Line Description	PTAE	PO Number
1	ITEM	504.00	08-Jun-20XX	JUL-20XX	10977-015, 300334, Water,Rnase free	1111111-1-AAAAA-11405	12345678
2	ITEM	485.00	08-Jun-20XX	JUL-20XX	25300-062, 300459, Trypsin/EDTA, 500ml	1111111-1-AAAAA-11405	12345678
3	ITEM	685.60	08-Jun-20XX	JUL-20XX	15520-034, 300460, X-gal 100mg	1111111-1-AAAAA-11405	12345678
4	ITEM	399.50	08-Jun-20XX	JUL-20XX	25530-015, 301267, Proteinase K, 100mg	1111111-1-AAAAA-11405	12345678
5	ITEM	249.00	08-Jun-20XX	JUL-20XX	A11122, 300042, Anti GFP rabbit IgG fraction	1111111-1-AAAAA-11405	12345678
6	TAX	187.52	08-Jun-20XX	JUL-20XX	8.25% SANTA CLARA & SAN MATEO COUNTY SALES TAX	1111111-1-AAAAA-11405	
<b>Invoice Total</b>		<b>2,460.62</b>					

  

**Payment Information**

Invoice Status	Invoice Holds	Check Number	Check Date	Date Check Cleared	Check Status
Due					

  

Document Name: FIN\_EXP\_138\_Invoice\_Detail\_Recon.rpt    Tab Name: Full Display

F: Sample Report 206 Purchase Order Detail

Stanford University Purchase Order Detail Report - Full Display										
PO Number: 12345678 Supplier Name : % From PO Create Date: % To PO Create Date: %							Page: 1 of 1 Run Date: 03-JUL-20XX User: QWD Database: Production			
# of PO Change Order	PO Number	PO Status	PO Creation Date	Supplier #	Supplier Name	PO Terms	FOB	Buyer	Ship To Address	
0	12345678	APPROVED	08-JUN-20XX	012345	SUPPLIER	N30	ORIGIN	Purchase Order, Rapid	Stanford Univ, 385 SERRA MALL HERRIN LABS	
PO Line #	PO Line Category	Supplier Item #	PO Line Item Description	Unit of Measure	Quantity	Unit Price	Extended Price	PO Line PTAE	Promise Date	Qty Rcvd
1	RPO GOODS	Bio Tech	10977-015, 300334, Water,Rnase free	EACH	60.00	8.40	504.00	1111111-1-AAAAA-11405		0
2	RPO GOODS	Bio Tech	25300-062, 300459, Trypsin/EDTA, 500ml	EACH	20.00	23.25	465.00	1111111-1-AAAAA-11405		0
3	RPO GOODS	Bio Tech	15520-034, 300460, X-gal 100mg	EACH	20.00	33.28	665.60	1111111-1-AAAAA-11405		0
4	RPO GOODS	Bio Tech	25530-015, 301267, Proteinase K, 100mg	EACH	5.00	77.90	389.50	1111111-1-AAAAA-11405		0
5	RPO GOODS	Bio Tech	A11122, 300042, Anti GFP rabbit IgG fraction	EACH	1.00	249.00	249.00	1111111-1-AAAAA-11405		0
Invoice Number	Invoice Date	Invoice Amount	Invoice Status	Check Date	Check Number	Check Status	Check Cleared Date			

Document Name: FIN\_PO\_206\_AP\_Purch\_Order\_Detail.rep - Full Display

**G: Sample Inventory Adjustment Journal**

Journal Number	ij0123456		Journal Type	New Journal					
Originator	Blaine, Rick		Status	Posted					
Period	JUN-20XX		Effective Date	20XX-07-02 00:00:00.0					
Title	Inventory Adjustment Journal								
Justification	This journal is adjusting the inventory asset as of June, 20XX based on a physical inventory count that was performed. The physical inventory count was valued at \$719,270.55. The General Ledger inventory at the end of the period was \$528,004.00, based on a Posted Journals report (#161) run for PTA 1234567-1-AAAAA, object code 11405, and period JUN-20XX. Inventory received but not included in the GL totalled \$200,924.27 that, when added to the GL inventory totalled \$728,928.27. The journal adjusts the GL inventory to match the physical count by reducing the GL inventory by \$9,657.72.								
<b>Line</b>	<b>Project</b>	<b>Task</b>	<b>Fund/ Award</b>	<b>Exp. Type</b>	<b>Exp. Date</b>	<b>Dept. Ref.</b>	<b>Debit</b>	<b>Credit</b>	<b>Description</b>
10	1234567	1	AAAAA	11405	30-JUN-20XX		0.00	9,657.72	Inventory 20XX
20	1234567	1	AAAAA	55950	30-JUN-20XX		9,657.72	0.00	Inventory 20XX
							9,657.72	9,657.72	
<b>Approver History</b>									
	<b>Action Date</b>	<b>Action</b>	<b>Name</b>		<b>Phone</b>	<b>Comments</b>			
0	20XX-07-01	Submitted	Originator, Journal		(650) 721-1111	Journal submitted for Approval			
1	20XX-07-01	Approved	Accountant, Store		(650) 722-2222				
2	20XX-07-02	Approved	Manager, Store		(650) 723-3333				
3	20XX-07-02	Approved	Manager, Business		(650) 724-4444				